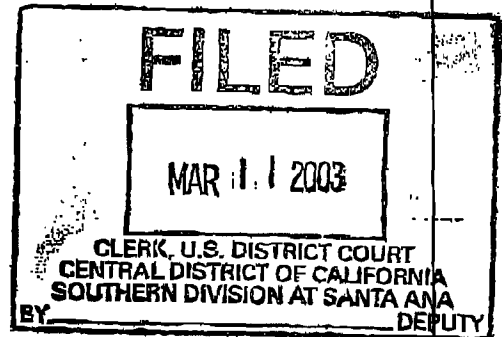


COPY

DEBRA W. YANG
United States Attorney
EDWARD M. ROBBINS, JR.
Assistant United States Attorney
Chief, Tax Division
ROBERT F. CONTE (SBN 157582)
Assistant United States Attorney
Room 7211 Federal Building
300 North Los Angeles Street
Los Angeles, California 90012
Telephone: (213) 894-6607
Facsimile: (213) 894-0115



W. CARL HANKLA
Trial Attorney, Tax Division
U.S. Department of Justice
P.O. Box 683, Ben Franklin Station
Washington, D.C. 20044
Telephone: (202) 307-6448
Facsimile: (202) 307-0054
w.carl.hankla@usdoj.gov

Attorneys for United States of America

UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

UNITED STATES OF AMERICA,
Plaintiff,
v.

SAMUEL J. DeANGELO; JOE
GORDON SHIELDS, a/k/a
GORDON SHIELDS; ALAN M.
HOVEY; JEFFREY R. WRIGHT;
KELLY DAVID, a/k/a DAVID
KELLY; and WESTERN TAX
SERVICES, INC.,

Defendants.

SA 03-0251 GLT
DECLARATION OF DAVID A. GORDON, MLGx
REVENUE AGENT

I, David A. Gordon, declare as follows:

- I am a Revenue Agent with the Internal Revenue Service, Small Business/Self Employed Division, Area 14 in Laguna Niguel, California. I have worked with the IRS since 1994.

1 I am currently assigned to the Abusive Schemes Group.

2 2. My official duties as a Revenue Agent include investigating
3 abusive schemes and/or tax shelter promotions that are
4 marketed/sold to individuals and legal entities by promising
5 favorable or improper tax benefits not allowed by the
6 Internal Revenue Code. My duties also include investigating
7 possible abusive schemes or systems used by professional
8 income tax return preparers (including those who aid or
9 assist in the preparation of returns) to understate the tax
10 liabilities of their customers in violation of the law.

11 OVERVIEW

12 3. The above-captioned case arose from a civil investigation I
13 was assigned to commence in August 2001 to investigate
14 whether the defendants were preparing federal income tax
15 returns in violation of the law at the offices of Western
16 Tax Service, Inc., located at 5757 E. La Palma, Anaheim,
17 California 92806. My conclusion is that the defendants have
18 violated and are continuing to violate the law by preparing
19 high numbers of income tax returns that willfully understate
20 their customers' tax liability. The defendants accomplish
21 this primarily through an abusive scheme of claiming bogus
22 itemized deductions for charitable contributions and
23 miscellaneous employee "business expenses", inserting false
24 or inflated figures on Schedule A of the returns so that the
25 tax liability is significantly reduced or eliminated and, in
26 over 90 percent of the cases, generating an undeserved or
27

inflated refund.

4. In connection with this investigation, the Internal Revenue Service has audited approximately 93 of the estimated 18,240 tax returns prepared by the defendants for the 2000-2002 tax seasons (that is, returns for tax years 1999-2001). Over 90 percent of these audited returns claimed false deductions for charitable contributions or employee business expenses, or both. Over 90 percent of these audited returns contained understatements of tax liability, the average tax loss being \$1,919.

5. Over 90 percent of the returns prepared by the defendants with respect to the years at issue claimed a refund. By comparison, of all Form 1040 returns filed nationwide, the proportion claiming refunds was significantly lower: 72.1 percent for 1999, 72 percent for 2000, and 76 percent for 2001.

6. The defendants' scheme avoids the attention of IRS information-matching programs. The returns the defendants prepare in most cases correctly reflect their customers' income information as reported to the IRS by third parties on Forms W-2 (wages) or Forms 1099, because omissions or inconsistencies would be obvious. Charitable contributions and employee business expenses are not subject to third-party reporting requirements, however, so the defendants can manipulate those deductions with much lower risk of attracting IRS notice.

7. The defendants failed to include the correct tax identification number on most of the returns they prepared during the 2000-2002 tax filing seasons. The identification number for Western Tax Service, Inc. (WTS) is 33-0895624. But most of the subject returns bore the number 95-3450380. The defendants' failure to include accurate tax identification numbers on the returns makes it more difficult for the IRS to keep track of their activity.

8. As a result of the improper returns prepared by the defendants, the United States has suffered a significant tax loss for tax years 1999-2001. The exact loss is unknown but can be reliably estimated. Given that the defendants prepared approximately 18,240 returns, and assuming, based on audits completed to date, that 90 percent of these returns contain understatements of tax, and assuming further, again based on audits to date, that the average tax loss per return is \$1,919, the resulting aggregate tax loss is estimated at \$31.5 million:

Tax Year	Understated Returns (Estimated)	Ave. Loss Per Return (Estimated)	Total Tax Loss (Estimated)
2001	90% of 5,262	\$1,919	\$ 9,088,000
2000	90% of 8,749	\$1,919	\$15,110,397
1999	90% of 4,229	\$1,919	\$ 7,303,905
			<u>\$31,502,302</u>

SCOPE AND METHODOLOGY OF IRS INVESTIGATION

- 1 9. I was assigned to commence this investigation in August 2001
2 after the IRS obtained certain records of Western Tax
3 Service, Inc. (WTS). WTS operates an income tax return
4 preparation business from its offices located at 5757 E. La
5 Palma Avenue, Anaheim, California 92807.
- 6 10. This investigation focuses on the 2000, 2001 and 2002 return
7 filing seasons, that is, federal income tax returns prepared
8 for tax years 1999, 2000 and 2001.
- 9 11. This investigation is based on the above-described records
10 obtained from WTS and other records obtained from the
11 defendants or their former customers, interviews conducted
12 with the individual defendants and their attorneys,
13 statements provided by or on behalf of the defendants,
14 statements provided by former customers of the defendants,
15 interviews with and statements provided by Marine attorneys
16 who reviewed income tax returns of enlisted personnel
17 prepared by the defendants, amended returns filed by Marine
18 customers to correct errors on the original returns prepared
19 by the defendants, IRS audits of income tax returns prepared
20 by the defendants, other IRS records, and other sources of
21 information. I have spent hundreds of hours working on this
22 case since it was opened.
- 23 12. In connection with this investigation, eleven other IRS
24 Revenue Agents and Tax Compliance Officers have completed
25 audits of approximately 93 of the income tax returns
26 prepared by the defendants for tax years 1999, 2000 and
27

1 2001. Other audits are ongoing. The IRS does not have the
2 resources to audit every one of the returns prepared by the
3 defendants.

4 13. The audits represent a wide range of incomes and
5 occupations, and includes taxpayers from Orange County, San
6 Diego, Los Angeles, and military bases in the area. The
7 results were consistent across the board. Accordingly, I
8 believe that the audited returns are fairly representative
9 of all the returns prepared by the defendants.

10 14. To date, the eleven Revenue Agents and Tax Compliance
11 Officers have spent hundreds of hours on these audits. A
12 single audit may take up to 18 hours to complete. Each
13 audit usually includes a face-to-face interview with the
14 customer.

15 15. In nearly every case where the defendants prepared a return
16 with a Schedule A, the audit revealed that the Schedule A
17 contained false or inflated itemized deductions for
18 charitable contributions and employee business expenses. In
19 nearly every such case, the customer has been unable to
20 substantiate these deductions during the audit. In fact, in
21 nearly every such case, the customer taxpayer has indicated
22 that the defendants included these bogus deductions on the
23 return without the customer's knowledge or consent.

24 16. In most cases, customers have agreed at the conclusion of
25 their audits to pay the correct tax due as determined by the
26 Revenue Agents or Tax Compliance Officers, plus interest as
27

1 required by law. Since many customers are not in a position
2 to pay the outstanding balance of their tax liabilities in a
3 lump sum, they have entered into installment agreements to
4 make payments each month.

5 THE DEFENDANTS

6 17. During my investigation, I learned that WTS is owned and
7 operated by Samuel J. DeAngelo. DeAngelo has been preparing
8 income tax returns for approximately 30 years. He
9 reportedly obtained an associate of arts degree in business
10 administration from Santa Ana College in 1972. He is not a
11 certified public accountant or an enrolled agent (enrolled
12 agents must pass an exam administered by the IRS to test
13 basic knowledge of tax law and administrative procedure, and
14 they are allowed to represent customers in proceedings
15 before the IRS).

16 18. In 1973, DeAngelo began his own income tax return
17 preparation business as a sole proprietorship known as
18 DeAngelo Tax Service (DTS). DTS operated out of DeAngelo's
19 home in Yorba Linda, California.

20 19. DeAngelo trained and employed other persons as tax return
21 preparers at DTS.

22 20. On or about January 25, 2000, DeAngelo incorporated his
23 business, changed its name to WTS and moved it into its
24 current office in Anaheim.

25 21. WTS has employed and continues to employ a number of
26 individuals as income tax return preparers. Among these
27

1 individuals are Jeffrey Wright, who is the president of WTS
2 and DeAngelo's son-in-law; Kelly David, who is the vice
3 president of WTS; and Alan Hovey. Gordon Shields formerly
4 worked as a WTS return preparer but now works with Tax
5 Matters, Inc. out of office at 12155 Magnolia Avenue, # 6G,
6 Riverside, California 92503.

7 22. Wright, David, Hovey and Shields all began their careers as
8 income tax return preparers under the training and
9 supervision of DeAngelo. None of these individuals is a
10 certified public accountant or an enrolled agent.

11 23. Preparers working under DeAngelo are expected to do business
12 strictly in accordance with his practices and procedures.
13 An internal WTS memo dated February 9, 2001, emphasized that
14 returns were to be prepared "Sam's way" and customers were
15 to be billed "Sam's way."

16 24. Shields represents himself as an enrolled agent. His status
17 as an enrolled agent was revoked in 1993.

18 HOW THE WTS TAX RETURN PREPARATION SCHEME WORKED

19 25. WTS operated, and continues to operate, a high-volume
20 business. In the 2000 return season (for preparing tax
21 returns for 1999), WTS prepared 4,229 returns; in the 2001
22 season, 8,749 returns; and in the 2002 season, 5,262
23 returns.

24 26. The defendants' typical customers have been middle-income
25 individual wage earners. Advertising is by word of mouth.
26 Customers are referred by friends or relatives who have
27
28

- 1 received tax refunds through the defendants.
- 2 27. WTS generally prepares each customer's return during a
3 single appointment lasting less than an hour, including
4 waiting time. Preparers often spend only a few minutes with
5 each customer.
- 6 28. When a customer arrives at WTS for an appointment, a support
7 staff member inputs information from the customer's Forms W-
8 2 or 1099 into a computer program. Sometimes the customer
9 will fax this information ahead of time. The customer then
10 waits to see a return preparer.
- 11 29. The preparer takes the customer to his or her office to
12 prepare the return using a computer terminal on the
13 preparer's desk. During the often very brief meeting with
14 the preparer, the preparer begins asking a series of yes-or-
15 no questions regarding church attendance, computer ownership
16 or use, use of car for work, and other questions regarding
17 charitable or job-related activities. Military customers
18 are even asked if they get haircuts.
- 19 30. The preparer does not make reasonable inquiries or otherwise
20 attempt to determine the actual amounts of the customer's
21 charitable contributions or deductible employee business
22 expenses. Nor does the preparer ask for or rely on any
23 substantiation for the contributions and job expenses
24 ultimately included on Schedule A of the return.
- 25 31. The preparer avoids allowing the customer to see the
26 computer screen as the preparer types in amounts for items
27
28

1 such as charitable contributions or business expenses. If
2 the customer requests to look, the preparer will refuse,
3 offering the excuse that the return is not completed.

4 32. The preparer does not take the time to explain the
5 individual line items on the return to the customer. In
6 particular, the preparer does not point out or explain the
7 bogus deductions for charitable contributions and employee
8 business expenses.

9 33. The bogus deductions are not obvious to the customers
10 because they are buried on Schedule A, which is an
11 attachment to the Form 1040. Further, the defendants often
12 do not complete the required Form 2106 to describe
13 unreimbursed employee business expenses.

14 34. After a return is completed on-screen by the preparer, the
15 preparer presumably has the customer sign it electronically
16 by entering a personal identification number (PIN) in the
17 computer or, in the alternative, has the customer sign a
18 one-page Form 8453 to authenticate the electronic portion of
19 the Form 1040. The customer is provided a copy of the
20 return at the conclusion of the appointment along with a
21 cover sheet showing the refund amount (or, to a far lesser
22 extent, the amount of tax due). The bogus deductions are
23 not highlighted.

24 35. The defendants charge their customers fees ranging from a
25 minimum of \$300 to \$3,000 or more. These fees are well over
26 what is customarily charged by professional return preparers
27

1 in the Orange County area to prepare correct returns for
2 similar taxpayers. A reasonable fee to prepare a Form 1040
3 for one of the defendants' typical wage-earner customers
4 should be well under \$300.

5 36. If customers inquire about the size of the fee charged, the
6 defendants state that the fee is based on a percentage of
7 the refund obtained for them.

8 37. The defendants generally file the returns electronically,
9 which ensures that customers will receive their refunds as
10 soon as possible. The returns are prepared with the
11 necessary information so that refunds will be deposited
12 directly into the customers' bank accounts.

13 38. Most customers are given the option of paying the fee by
14 tendering a check post-dated to when the refund is expected.
15 Thus these customers can have their returns prepared without
16 having to pay any funds out of pocket.

17 39. In nearly every case audited to date, the defendants have
18 improperly inflated the customer's actual charitable
19 contributions.

20 40. In nearly every case audited to date, the defendants have
21 improperly claimed nondeductible employee business expenses.
22 Most customers have not been legally entitled to itemize any
23 employee business expenses or other expenses such as
24 depreciation on office equipment on Schedule A of Form 1040
25 because the customers did not actually expend the amounts
26 claimed and/or they were not eligible to claim them under
27

1 the circumstances. The preparer more often should have
2 claimed the standard deduction instead of itemizing on a
3 Schedule A.

4 41. In nearly every case audited to date, the defendants'
5 improper deductions have been sufficient in amount to create
6 a refund of federal tax large enough to pay the defendants'
7 fee and leave an excess for the customer.

8 42. Attached hereto as **Exhibit 1** is a true copy of a spreadsheet
9 I prepared showing the results of 56 completed audits of
10 returns prepared by WTS. Social security numbers and other
11 irrelevant information has been redacted.

12 43. Attached hereto as **Exhibit 2** is a true copy of a spreadsheet
13 I prepared showing the results of an additional 37 completed
14 audits of returns prepared by WTS. Ongoing audits are also
15 reflected on the return. Social security numbers and other
16 irrelevant information has been redacted.

17 PARTICULAR CUSTOMERS

18 *Hugo Hernandez and Ana L. Hernandez*

19 44. On April 12, 2001, Hugo Hernandez, referred to WTS by a
20 family member, went to WTS' offices in Anaheim to have his
21 and his wife Ana's 2000 joint tax return prepared. See
22 Declaration of Hugo Hernandez, a true copy of which is
23 attached hereto as **Exhibit 3**. The Hernandezes live in
24 Covina, California. Mr. Hernandez is a network engineer for
25 Southern California Edison, and Mrs. Hernandez works as an
26 office administrator. Together, they had taxable wages of
27
28

\$83,368 for year 2000.

45. Mr. Hernandez met with David for approximately 20 minutes. David asked Mr. Hernandez whether he made charitable contributions during the year or incurred any business expenses. Mr. Hernandez told David that he made contributions to his church but incurred no expenses with respect to his employment. David prepared a tax return that claimed bogus charitable contributions of \$7,800 and bogus employee business expenses of \$8,114. Mr. Hernandez did not provide these figures to David.

46. Mr. Hernandez was charged \$1,500 for preparation of the tax return, which claimed a refund of \$2,695. When Mr. Hernandez questioned the amount of the fee, David told him that "WTS charges what they charge because they are the best and if [he] went somewhere else, [he] would have owed taxes." Mr. Hernandez paid the fee with a post-dated check based on the anticipated date of receipt of the refund.

47. David also prepared the Hernandezes' 2001 return. It resulted in a refund of \$705.

48. The IRS has audited the Hernandezes' 2000 and 2001 tax returns. The examination concluded that the Hernandezes owed \$5,094 of tax and interest for those years. The Hernandezes agreed to this liability.

49. A copy of the 2000 Form 1040 return prepared by David for the Hernandezes is attached as **Exhibit 4**. The social security numbers and the bank account/routing numbers have

1 been blacked out, but otherwise the return is as filed. It
2 was filed electronically, so there are no signatures on the
3 return.

4 50. The bogus deductions appear as part of the total itemized
5 deductions of \$31,784 listed on line 36 of the Form 1040.
6 The bogus deductions improperly reduced the Hernandezes'
7 taxable income to make it appear that no tax was due and a
8 refund of \$2,695 was owing. The refund is shown on lines 66
9 and 67a of the return.

10 51. The itemized deductions on line 36 of the Form 1040 are
11 broken down on Schedule A. The relevant sections of
12 Schedule A are titled "Gifts to Charity," beginning at line
13 15, and "Job Expenses and Most Other Miscellaneous
14 Deductions," beginning at line 20.

15 52. Line 15 of Schedule A reveals \$7,800 claimed for charitable
16 gifts by cash or check. It is unknown how David arrived at
17 this figure. Mr. Hernandez did not provide it to him. The
18 \$7,800 is carried over to line 18 in the right hand margin
19 to become a component of the total itemized deductions of
20 \$31,784 on line 28 of Schedule A, which in turn is carried
21 over to line 36 of Form 1040.

22 53. Line 22 of Schedule A reveals "Business expenses" of \$8,114
23 and "Depreciation" of \$2,200. This resulted in the total of
24 \$10,314 on line 22. Since such expenses are deductible only
25 to the extent they exceed 2 percent of adjusted gross
26 income, the \$10,314 was reduced by \$1,678 and carried over
27

1 to line 26 in the right hand margin as an \$8,636 item. The
2 expenses of \$8,636 thus became a component of the total
3 itemized deductions of \$31,784 on line 28 of Schedule A,
4 which in turn is carried over to line 36 of Form 1040.

5 54. The return does not contain a breakdown of the "Business
6 expenses" of \$8,114. Employee business expenses are
7 supposed to be listed on a Form 2106, which is supposed to
8 be attached to the Form 1040. David did not do this when
9 preparing the return.

10 55. It is unknown how David arrived at the \$8,114 figure for
11 business expenses. At any rate, the Hernandezes had no
12 expenses that fell into the category of deductible employee
13 business expenses. To be deductible, such expenses must be
14 incurred as a condition of employment.

15 56. The return does contain a partial description of the \$2,200
16 "Depreciation" expense. This is on Form 4562 attached to
17 Form 1040. The description is "5-Year COMPUTER." Although
18 the Hernandezes owned a computer, it did not meet the
19 requirements for a deductible employee business expense.
20 The Hernandezes were not required to purchase their computer
21 as a condition of employment. It was not proper for David
22 to claim any portion of the cost of the computer as
23 deductible depreciation.

24 57. If David had not claimed the bogus deductions, the
25 Hernandezes' return would have reported \$3,832 in tax
26 instead of the \$2,695 refund claim David inserted.

Michele Gonzalez

58. In February 2001, Michele Gonzalez went to WTS to have her 2000 tax return prepared. See Declaration of Michele Gonzalez, a true copy of which is attached hereto as **Exhibit 5**. She lives in San Jacinto, California. She is employed as a meat clerk with Stater Brothers Markets. She had taxable wages of \$27,393 for year 2000.
59. Ms. Gonzalez met with Hovey for approximately 5 minutes. Hovey asked her if she attended church (which she did) and asked if she had bought a computer (which she had). Hovey prepared a tax return that claimed false charitable contributions of \$2,600 and false employee business expenses of \$10,927. She did not provide those figures to Hovey.
60. Ms. Gonzalez was charged \$500 for the tax return, which claimed a refund of \$1,953.
61. The IRS has audited Ms. Gonzalez's 2000 tax return and determined additional tax and interest due in the amount of \$1,734. Ms. Gonzalez agreed to this liability.
62. A copy of Ms. Gonzalez's 2000 Form 1040 return is attached as **Exhibit 6**. The social security number and the bank account/routing numbers have been blacked out, but otherwise the return is as filed. It was filed electronically, so there are no signatures on the return.
63. The bogus deductions appear as part of the total itemized deductions of \$14,783 listed on line 36 of the Form 1040. The bogus deductions improperly reduced Ms. Gonzalez's

1 taxable income to make it appear that no tax was due and a
2 refund of \$1,953 was owing. The refund is shown on lines 66
3 and 67a of the return.

4 64. The itemized deductions on line 36 of the Form 1040 are
5 broken down on Schedule A. The relevant sections of
6 Schedule A are titled "Gifts to Charity," beginning at line
7 15, and "Job Expenses and Most Other Miscellaneous
8 Deductions," beginning at line 20.

9 65. Line 15 of Schedule A reveals \$2,600 claimed for charitable
10 gifts by cash or check. It is unknown how Hovey arrived at
11 this figure. Ms. Gonzalez did not provide it to him. The
12 \$2,600 is carried over to line 18 in the right hand margin
13 to become a component of the total itemized deductions of
14 \$14,783 on line 28 of Schedule A, which in turn is carried
15 over to line 36 of Form 1040.

16 66. Line 22 of Schedule A reveals "Business Expenses" of
17 \$10,927. Along with union dues of \$322 and tax return
18 preparation fees of \$500 for the previous year, the total
19 expenses were \$11,749, on line 23. Such expenses are
20 deductible only to the extent they exceed 2 percent of
21 adjusted gross income, so the \$11,749 was reduced by \$558
22 and carried over to line 26 in the right hand margin as an
23 \$11,191 item. The \$11,191 thus became a component of the
24 total itemized deductions of \$14,783 on line 28 of Schedule
25 A, which in turn is carried over to line 36 of Form 1040.

26 67. The return does not contain a breakdown of the "Business
27
28

1 expenses" of \$10,927. Employee business expenses are
2 supposed to be listed on a Form 2106, which is supposed to
3 be attached to the Form 1040. Hovey did not do this when
4 preparing the return.

5 68. It is unknown how Hovey arrived at the \$10,927 figure for
6 business expenses. At any rate, Ms. Gonzalez had no
7 expenses that fell into the category of deductible employee
8 business expenses. To be deductible, such expenses must be
9 incurred as a condition of employment and must exceed 2
10 percent of adjusted gross income.

11 69. If Hovey had not claimed the bogus deductions, Ms.
12 Gonzalez's return would have reported \$1,552 in tax instead
13 of the \$1,953 refund claim Hovey inserted.

14 *Elama J. Pele and Lori Lisa Lynn-Pele*

15 70. On April 14, 2001, Lori Pele, referred to WTS by a family
16 member, went to WTS to have her 2000 joint tax return
17 prepared. See Declaration of Lori Pele, a true copy of
18 which is attached hereto as **Exhibit 7**. She and her husband
19 live in San Diego, California. She is a social worker at
20 Children's Hospital. Her husband is with a security firm.
21 Together, they had taxable wages of \$65,196 for 2000.

22 71. Ms. Pele met with Wright for approximately 10 minutes. She
23 told Wright she made non-cash charitable contributions of
24 \$3,500 to the Salvation Army. Wright asked her whether she
25 had a computer, a desk, chairs, and a bookshelf at home
26 (which she did). Wright incorrectly told the customer she
27

1 could deduct these items because she took work home at
2 night. Wright prepared a tax return showing inflated
3 charitable contributions of \$6,500 and bogus employee
4 business expenses of \$15,173. Ms. Pele did not provide
5 these figures to Wright.

6 72. Ms. Pele was charged \$1,050 for preparing the return, which
7 claimed a refund of \$3,310.

8 73. The IRS has audited the Peles' joint 2000 tax return and has
9 determined additional tax and interest due in the amount of
10 \$4,568. The Peles agreed to this liability.

11 74. A copy of the 2000 Form 1040 return prepared by Wright for
12 the Peles is attached as **Exhibit 8**. The social security
13 numbers and the bank account/routing numbers have been
14 blacked out, but otherwise the return is as filed. It was
15 filed electronically, so there are no signatures on the
16 return.

17 75. The bogus deductions appear as part of the total itemized
18 deductions of \$28,098 listed on line 36 of the Form 1040.
19 The bogus deductions improperly reduced the Peles' taxable
20 income to make it appear that no tax was due and a refund of
21 \$3,310 was owing. The refund is shown on lines 66 and 67a
22 of the return.

23 76. The itemized deductions on line 36 of the Form 1040 are
24 broken down on Schedule A. The relevant sections of
25 Schedule A are titled "Gifts to Charity," beginning at line
26 15, and "Job Expenses and Most Other Miscellaneous
27
28

1 Deductions," beginning at line 20.

2 77. Line 15 of Schedule A reveals \$6,500 claimed for charitable
3 gifts by cash or check. It is unknown how Wright arrived at
4 this figure. Ms. Pele did not provide it to him; she told
5 him that she made \$3,500 in non-cash contributions. The
6 \$6,500 is carried over to line 18 in the right hand margin
7 to become a component of the total itemized deductions of
8 \$28,098 on line 28 of Schedule A, which in turn is carried
9 over to line 36 of Form 1040.

10 78. Line 22 of Schedule A reveals "Business expenses" of \$15,173
11 and "Depreciation" of \$4,250. This accounted for most of
12 the total of \$19,673 on line 22. Since such expenses are
13 deductible only to the extent they exceed 2 percent of
14 adjusted gross income, the \$19,673 was reduced by \$1,284 and
15 carried over to line 26 in the right hand margin as an
16 \$18,389 item. The expenses of \$18,389 thus became a
17 component of the total itemized deductions of \$28,098 on
18 line 28 of Schedule A, which in turn is carried over to line
19 36 of Form 1040.

20 79. The return does not contain a breakdown of the "Business
21 expenses" of \$15,173. Employee business expenses are
22 supposed to be listed on a Form 2106, which is supposed to
23 be attached to the Form 1040. Wright did not do this when
24 preparing the return.

25 80. It is unknown how Wright arrived at the \$15,173 figure for
26 business expenses. At any rate, the Peles had no expenses
27

1 that fell into the category of deductible employee business
2 expenses. To be deductible, such expenses must be incurred
3 as a condition of employment.

4 81. The return does contain a partial description of the \$4,250
5 "Depreciation" expense. This is on Form 4562 attached to
6 Form 1040. The description is "5-Year COMPUTER/Equipment."
7 Although the Peles owned a computer, it did not meet the
8 requirements for a deductible employee business expense.
9 They were not required to purchase their computer as a
10 condition of employment. It was not proper for Wright to
11 claim any portion of the cost of the computer as deductible
12 depreciation.

13 82. If Wright had not claimed the bogus deductions, the Peles'
14 return would have reported \$4,078 in tax instead of the
15 \$3,310 refund claim Wright inserted.

16 *Kerry M. Issel and Richard A. Issel*

17 83. On March 30, 2001, Kerry and Richard Issel, referred to WTS
18 by a co-worker of Kerry's, went to WTS to have their 2000
19 joint tax return prepared. See Declaration of Kerry Issel,
20 a true copy of which is attached hereto as **Exhibit 9**. Ms.
21 Issel was told by her co-worker that WTS would get her a big
22 refund. The Issels live in Chino Hills, California. She is
23 an ultrasound technician. He is currently disabled and not
24 working. Together, they had taxable income of \$55,347 for
25 2000.

26 84. The Issels met with Shields. Shields asked the Issels if
27
28

1 they owned a home computer and any office furniture at home
2 (which they did). Shields did not ask them when the items
3 were purchased or what they cost. Shields prepared a tax
4 return claiming \$1,000 in false charitable contributions and
5 \$13,005 of bogus employee business expenses.

6 85. The Issels were charged \$1,500 for the return preparation.
7 The return claimed a refund of \$7,559.

8 86. The IRS audited the tax return and has determined that
9 additional tax and interest in the amount of \$8,884 is due.
10 The Issels agreed to this liability.

11 87. A copy of the 2000 Form 1040 return prepared by Shields for
12 the Issels is attached as **Exhibit 10**. The social security
13 numbers and the bank account/routing numbers have been
14 blacked out, but otherwise the return is as filed. It was
15 filed electronically, so there are no signatures on the
16 return.

17 88. The bogus deductions appear as part of the total itemized
18 deductions of \$45,617 listed on line 36 of the Form 1040.
19 The bogus deductions improperly reduced the Issels' taxable
20 income to make it appear that no tax was due and a refund of
21 \$7,559 was owing. The refund is shown on lines 66 and 67a
22 of the return.

23 89. The itemized deductions on line 36 of the Form 1040 are
24 broken down on Schedule A. The relevant sections of
25 Schedule A are titled "Gifts to Charity," beginning at line
26 15, and "Job Expenses and Most Other Miscellaneous
27
28

1 Deductions," beginning at line 20.

2 90. Line 15 of Schedule A reveals \$500 claimed for charitable
3 gifts by cash or check, and line 16 contains \$500 for gifts
4 other than by cash or check. It is unknown how Shields
5 arrived at these figures. The Issels did not provide them
6 to him. The \$1,000 total is carried over to line 18 in the
7 right hand margin to become a component of the total
8 itemized deductions of \$45,617 on line 28 of Schedule A,
9 which in turn is carried over to line 36 of Form 1040.

10 91. Line 22 of Schedule A reveals "Business expenses" of \$13,005
11 and "Depreciation" of \$12,635. This resulted in the total
12 of \$25,640 on line 22. Since such expenses are deductible
13 only to the extent they exceed 2 percent of adjusted gross
14 income, the \$25,640, plus \$45 in union dues, was reduced by
15 \$1,390 and carried over to line 26 in the right hand margin
16 as a \$24,295 item. The expenses of \$24,295 thus became a
17 component of the total itemized deductions of \$45,617 on
18 line 28 of Schedule A, which in turn is carried over to line
19 36 of Form 1040.

20 92. The return does not contain a breakdown of the "Business
21 expenses" of \$13,005. Employee business expenses are
22 supposed to be listed on a Form 2106, which is supposed to
23 be attached to the Form 1040. Shields did not do this when
24 preparing the return.

25 93. It is unknown how Shields arrived at the \$13,005 figure for
26 business expenses. At any rate, the Issels had no expenses
27

1 that fell into the category of deductible employee business
2 expenses. To be deductible, such expenses must be incurred
3 as a condition of employment.

4 94. The return does contain a partial description of the \$12,635
5 "Depreciation" expense. This is on Form 4562 attached to
6 Form 1040. The description is "5-Year COMPUTERS 2," \$4,800,
7 and "5-Year EQUIPMENT," \$7,835. Although the Issels owned a
8 computer and office equipment, they did not meet the
9 requirements for a deductible employee business expense.
10 The Issels were not required to purchase their computer and
11 equipment as a condition of employment.

12 95. If Shields had not claimed the bogus deductions, the Issels'
13 return would have reported \$7,949 in tax instead of the
14 \$7,559 refund claim Shields inserted.

15 *Jacqueline Fontanez*

16 96. On February 18, 2000, Jacqueline Fontanez, referred by a
17 friend, went to DTS to have her 1999 tax return prepared.
18 See Declaration of Jacqueline Fontanez, a true copy of which
19 is attached hereto as **Exhibit 11**. Ms. Fontanez is a
20 reservations supervisor with Quantas Vacations. She lives
21 in Los Angeles. She had taxable wages of \$28,577 for 1999.

22 97. Ms. Fontanez met with DeAngelo. He asked her whether she
23 made charitable contributions (which she did, in modest
24 amounts to her church) and whether she owned a home computer
25 (which she did). She told DeAngelo that she did not have
26 receipts to show the amount of her contributions or the cost
27
28

1 of the computer. DeAngelo told the customer how to create
2 receipts if ever audited by the IRS. DeAngelo prepared a
3 tax return showing false charitable contributions of \$2,600
4 and false employee business expenses of \$13,895.

5 98. Ms. Fontanez was charged \$550 for preparation of her tax
6 return, which claimed a refund of \$2,333.

7 99. The IRS audited the return and has determined that
8 additional tax and interest is due in the amount of \$5,827.
9 Ms. Fontanez agreed to this liability.

10 100. A copy of the 1999 Form 1040 return prepared by DeAngelo for
11 Ms. Fontanez is attached as **Exhibit 12**. The social security
12 numbers and the bank account/routing numbers have been
13 blacked out, but otherwise the return is as filed.

14 101. The bogus deductions appear as part of the total itemized
15 deductions of \$19,956 listed on line 36 of the Form 1040.
16 The bogus deductions improperly reduced Ms. Fontanez's
17 taxable income to make it appear that no tax was due and a
18 refund of \$2,333 was owing. The refund is shown on lines 66
19 and 67a of the return.

20 102. The itemized deductions on line 36 of the Form 1040 are
21 broken down on Schedule A. The relevant sections of
22 Schedule A are titled "Gifts to Charity," beginning at line
23 15, and "Job Expenses and Most Other Miscellaneous
24 Deductions," beginning at line 20.

25 103. Line 15 of Schedule A reveals \$2,600 claimed for charitable
26 gifts by cash or check. It is unknown how DeAngelo arrived
27
28

1 at this figure. Ms. Fontanez did not provide it to him.
2 The \$2,600 is carried over to line 18 in the right hand
3 margin to become a component of the total itemized
4 deductions of \$19,956 on line 28 of Schedule A, which in
5 turn is carried over to line 36 of Form 1040.

6 104. Line 22 of Schedule A reveals "Business expenses" of \$13,895
7 and "Depreciation" of \$2,250. This resulted in the total of
8 \$16,145 on line 22. There were also tax preparation fees of
9 \$550 claimed on line 21. Since such expenses are deductible
10 only to the extent they exceed 2 percent of adjusted gross
11 income, the \$16,695 total on line 23 was reduced by \$578 and
12 carried over to line 26 in the right hand margin as a
13 \$16,117 item. The expenses of \$16,117 thus became a
14 component of the total itemized deductions of \$19,956 on
15 line 28 of Schedule A, which in turn is carried over to line
16 36 of Form 1040.

17 105. The return does not contain a breakdown of the "Business
18 expenses" of \$13,895. Employee business expenses are
19 supposed to be listed on a Form 2106, which is supposed to
20 be attached to the Form 1040. DeAngelo did not do this when
21 preparing the return.

22 106. It is unknown how DeAngelo arrived at the \$13,895 figure for
23 business expenses. At any rate, Ms. Fontanez had no
24 expenses that fell into the category of deductible employee
25 business expenses. To be deductible, such expenses must be
26 incurred as a condition of employment.

1 107. The return does contain a partial description of the \$2,250
2 "Depreciation" expense. This is on Form 4562 attached to
3 Form 1040. The description is "5-Year Office." Although
4 Ms. Fontanez owned a computer and office equipment, she did
5 not meet the requirements for a deductible employee business
6 expense. She was not required to purchase these items as a
7 condition of employment. It was not proper for DeAngelo to
8 claim any portion of their cost as deductible depreciation.

9 108. If DeAngelo had not claimed the bogus deductions, Ms.
10 Fontanez' return would have reported \$2,348 in tax instead
11 of the \$2,333 refund claim DeAngelo inserted.

12 ADDITIONAL INDIVIDUAL CUSTOMERS

13 109. Attached hereto as **Exhibits 13 through 17** are true copies of
14 the Declarations of several other individual customers of
15 WTS: Eva C. Marez, Maria Carolina Flint, Leah Spann, Owen
16 Williams, and Marcial Bio. These Declarations describe
17 experiences similar to those found in the Declarations of
18 Hugo Hernandez, Michele Gonzalez, Lori Pele, Kerry Issel,
19 and Jacqueline Fontanez discussed above. In each case, one
20 of the individual defendants prepared a return containing
21 bogus charitable contributions and employee business
22 expenses in amounts sufficient to create an undeserved
23 refund, and in each case, the IRS audited the return and
24 determined a deficiency in tax due.

25 U.S. MARINE CORPS ENLISTED PERSONNEL

26 110. By their proximity to the now-closed El Toro Marine Corps
27
28

1 Base in Orange County, California, and through word-of-
2 mouth, the defendants managed to target military personnel
3 in Orange County and San Diego County, California, with
4 their false tax return preparation scheme. During the 2000
5 and 2001 tax return filing seasons, it is estimated that
6 DTS/WTS personnel prepared returns for well over one hundred
7 enlisted men and women. These tax returns, like the other
8 tax returns prepared by DTS/WTS, reflected an abusive
9 pattern of claiming bogus itemized deductions for charitable
10 contributions and employee business expenses.

11 111. During the 2001 tax return preparation season, Marine Lt.
12 Col. Sheila Bryant-Tucker was the Internal Revenue Service-
13 Volunteer Income Tax Assistance (VITA) Coordinator for the
14 Marine Corps Base at Camp Pendleton, California. A copy of
15 an affidavit signed by Lt. Col. Bryant-Tucker is attached
16 hereto as **Exhibit 18**. As described in the affidavit, it
17 came to Lt. Col. Bryant-Tucker's attention from one of the
18 lead VITA tax preparers that WTS had claimed incorrect
19 deductions on Corporal Angela Rouse's return in order to
20 generate an inflated refund. VITA assisted Corporal Rouse
21 in filing an amended return. Other Marines who came in to
22 VITA to have their returns amended reported similar
23 experiences with WTS.

24 112. Capt. Eric E. Weiss was the Officer in Charge (OIC) of VITA
25 at Camp Pendleton during the 2001 tax season. A copy of his
26 affidavit is attached hereto as **Exhibit 19**. He was

1 contacted by Capt. Jerry Stevenson, who was the OIC of VITA
2 at Miramar Marine Corps Air Station in San Diego. Capt.
3 Stevenson advised him of a "scam" involving potentially
4 hundreds of returns prepared by WTS for Marines. A few days
5 later, several Marines came into the VITA office at Camp
6 Pendleton with questions about their year 2000 returns,
7 which recently had been prepared by WTS. They reported that
8 WTS had asked them questions such as "Do you buy uniform
9 items?" and then had claimed "huge numbers (\$500-\$1,500)
10 without asking how much was spent." This resulted in
11 improper "miscellaneous" deductions claimed on Schedule A of
12 the returns. VITA then sent out an e-mail message to all
13 personnel on the base, which resulted in approximately
14 twenty Marines coming into the VITA office with similar
15 returns prepared by WTS. According to Capt. Weiss, the
16 number \$1,040 was used as a deduction amount on at least
17 five of the returns. The Marines said that the preparers
18 never asked for figures to claim as deductions; the
19 preparers came up with their own. According to Capt. Weiss,
20 the Marines incorrectly assumed that WTS had allowed them
21 "standard amounts" for these deductions.

22 113. Following communications among the VITA officers at Miramar
23 and Camp Pendleton, it was decided to place articles in
24 military newspapers to warn military personnel to be on the
25 alert for tax preparers promising large refunds. An article
26 entitled "Firm allegedly cheats on Marine tax refunds" was
27

published in the military newspaper on Camp Pendleton about an Orange County tax return preparation firm obtaining false refunds for Marines. A true copy of the copy of that article found among the records obtained from WTS in June 2001, is attached hereto as **Exhibit 20**.

114. Capt. Stevenson arranged for several Marines who had their returns prepared by WTS to be audited by the IRS.

115. Attached hereto as **Exhibit 21** is a true copy of a spreadsheet I prepared reflecting amended returns filed by Marines with the assistance of VITA. The spreadsheet shows that each return prepared by WTS understated the correct tax due and claimed an inflated refund.

THREAT OF CONTINUING HARM

116. During the 2002 return preparation season, the defendants continued to prepare federal income tax returns with improper charitable contributions and employee business expenses. To date, audits of several Forms 1040 the defendants prepared for tax year 2001 have resulted in adjustments to these items. See **Exhibit 1** (Spreadsheet 2: Andrew Muchmore; see columns 4 (tax year) and 17 (adjustments to miscellaneous expenses)), **Exhibit 2** (Spreadsheet 3: Hugo Hernandez, Maria Gavino, Owen Williams, Victor Rodriguez, Antonio Orozco; see columns I (tax year), X (adjustments to charitable contributions) and Y (adjustments to miscellaneous expenses)).

117. The defendants are still in business. WTS still operates

1 from its offices at 5757 E. La Palma Avenue in Anaheim,
2 where DeAngelo, Wright, David and Hovey work. Shields still
3 does business from the office of Tax Matters, Inc., at 12155
4 Magnolia Avenue, #6G, in Riverside.

5 118. It is my belief that, based on the defendants' consistent
6 pattern of conduct over the years, that they are continuing
7 their abusive scheme of preparing tax returns with bogus
8 deductions for charitable contributions and miscellaneous
9 Schedule A "business expenses."

10 119. The defendants have a powerful financial incentive for
11 continuing to do business as usual. Through their
12 reputation for obtaining refunds, and through their policy
13 of allowing customers to defer payment until they receive
14 their refunds, the defendants have been able to charge fees
15 well in excess of what is reasonable.

16 120. WTS's records show that it grossed the following fees for
17 return preparation for the relevant tax seasons:

Tax Season	Tax Year	Revenue Earned by DTS/WTS
2001	2000	\$6.1 million (Jan. 2001-Jun. 2001)
2000	1999	\$2.8 million
1999	1998	\$1.3 million

23 121. During the current tax season, WTS has sent out a letter to
24 customers boasting of its "aggressive nature" in claiming
25 deductions. A true copy of this letter, dated January 15,
26 2003, is attached hereto as **Exhibit 22**. The letter
27

1 emphasizes that, "as always," WTS stands ready to help
2 customers claim "every possible deduction." But only two
3 deductions are mentioned by name--charitable contributions
4 and business expenses (*italics added*):

5 We at Western Tax Service, as always are
6 here to help you with *every possible*
7 *deduction* that you are legally entitled to
8 and because of this *aggressive nature* we need
9 to make sure that we fully document all of
10 your deductions. This includes
11 *contributions, business expenses, etc.*

12 122. WTS has sent out another letter, dated January 1, 2003,
13 containing instructions to customers who have been selected
14 for an IRS audit. A true copy of that letter is attached
15 hereto as **Exhibit 23**.

16 123. The January 1, 2003 letter advises customers about defending
17 their charitable contributions and employee "business
18 expenses."

19 124. Specifically, the January 1, 2003 letter provides detailed
20 guidelines for creating receipts and other documentation
21 after the fact to support the deductions for charitable
22 contributions and employee business expenses taken on
23 returns prepared by WTS.

24 125. To the extent the January 1, 2003 letter suggests that
25 creating such receipts and other documentation is acceptable
26 way of substantiating deductions on prior returns, it is
27 improper. The necessary substantiation to support a
28 deduction generally should exist at the time the return is
prepared.

126. For example, to substantiate a deduction on a prior year's return for automobile expenses, it is not proper to "recreate a mileage log" as advised in the January 1, 2003 letter. Regularly kept contemporaneous records are generally necessary for that purpose.

127. The January 1, 2003 letter is misleading in other respects. Using a table listing numerous examples, it indicates that deductions for in-kind charitable contributions (for example, contributions of clothing or household items to Goodwill) may be taken at original cost rather than at fair market value at the time of contribution:

Item	Cost
12 boxes of clothing	3,600
1 couch	825
1 mountain bike	300
1 Maytag washer & dryer	1,050
1 bedroom set	2,000
4 lamps	400
1 32" Hitachi television	675
1 Sony stereo system	500
7 suits	2,400
25 pairs of shoes	650
1 dishware set	425
	Total

See Exhibit 23. Using acquisition cost rather than fair market value at time of contribution would nearly always significantly overstate the allowable amount of the

1 deduction.

2 128. Further, the January 1, 2003 letter represents that
3 customers can validly create and sign their own receipts for
4 charitable contributions in excess of \$250, providing
5 suggested language ("I, John Doe, gave Calvary Chapel of
6 Costa Mesa \$2,500.00 for the 2000 year"). See Exhibit 23.
7 This is incorrect advice. Contributions of \$250 or more are
8 deductible only if substantiated by a acknowledgment of the
9 contributions from the qualified organization or certain
10 payroll deduction records.

11 129. The January 1, 2003 letter also implies that computers and
12 other home office equipment can be depreciated and deducted
13 as miscellaneous Schedule A "business expenses" if the
14 customer uses them even occasionally for business purposes
15 ("Depreciation relates to an item that you either purchased
16 or placed in service that year which you use for business
17 purposes such as a computer or office equipment"). See
18 **Exhibit 23.** That is not the law. Such items are deductible
19 only if their use is for the convenience of the employer and
20 required as a condition of employment.

21 130. If the defendants are not enjoined from preparing income tax
22 returns, it is my opinion, based on the facts set forth in
23 this declaration, that the defendants will continue to
24
25
26
27
28


1 prepare false and fraudulent tax returns, understating their
2 clients' tax liability through the use of bogus deductions
3 for charitable contributions and miscellaneous "business
4 expenses." (The defendants may also be engaging in other
5 abusive schemes as well; with respect to the 1999 tax year,
6 DeAngelo claimed a bogus "slave reparation credit" of
7 \$40,000 on behalf of an African-American client.)

8 131. Allowing the defendants to continue doing business as usual
9 will result in a continuing and severe loss of tax revenue.
10 It will result in a continuing strain on IRS resources,
11 because we cannot audit every return the defendants prepare.
12 And it will cause financial hardship to clients who will be
13 audited--many will be required to pay unexpected tax
14 liabilities, including interest accruing from the due date
15 of the return to the date of payment.

16 132. In sum, allowing the defendants to continue doing business
17 as usual will cause further substantial interference with
18 the proper administration of the internal revenue laws.

19 I HEREBY DECLARE under penalty of perjury that the foregoing
20 is true and correct.

21 EXECUTED on this 5th day of March, 2003.

22
23 
24 DAVID A. GORDON
25 Revenue Agent
26 Internal Revenue Service
27 Abusive Schemes Group, Area 14
28